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No. 454

Supreme Court of the United States

OCTOBER TERM, 1925.

LEO A. PRICE, as Receiver in Equity of J. M. Gidding & Co., Inc.,

Petitioner,

against

UNITED STATES OF AMERICA,

Respondent.

BRIEF FOR PETITIONER

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Supreme Court of the United States

LEO A. PRICE, as Receiver in Equity of J. M. Gidding & Co., Inc., Petitioner, *against* UNITED STATES OF AMERICA, Respondent.	No. 454

BRIEF FOR PETITIONER.

This case comes here upon a writ of *certiorari* issued to the Circuit Court of Appeals for the Second Circuit, which court affirmed a decree of the United States District Court for the Southern District of New York. The decree of the District Court in turn affirmed a report of the Special Master, who recommended that claims of the United States for income taxes and for duties which accrued prior to the appointment of an equity receiver were entitled to prior payment in the distribution of the corporate assets. The decision below, 6 Fed. (2d) 758, was based on the opinion in *Liberty Mutual Insurance Co.* vs. *Johnson Shipyards* reported in 6 Fed (2d) 752 and annexed to the petition for the writ of *certiorari* herein. That case is also here on *certiorari* under the title of *Stripe, Receiver,* vs. *United States.*

The Question Presented.

The question presented is whether income taxes and duties payable for a period prior to the appointment of the receiver in equity are entitled to payment before the

debts due ordinary creditors. Specifically, the questions are:

(1) Is a claim for taxes and duty an indebtedness or a "debt" within the meaning of Section 3466 of the Revised Statutes?

(2) If it is, such an indebtedness, is the United States entitled to priority therefor in an equity receivership? That is, has the debtor been divested of its property in one of the methods specified in Section 3466?

(3) If the claim for taxes and duties is not within the purview of Section 3466 or if Section 3466 does not give it priority in an equity receivership, has the United States nevertheless an inherent sovereign right of priority for the payment of taxes and duties?

Statement of Facts.

This is the usual suit brought by a common contract creditor against a corporation to conserve and marshal the corporate assets in which the obtaining of a judgment by the plaintiff is waived by the defendant corporation by admitting the allegations of the bill and consenting to the appointment of a receiver (R. fol. 25). In the present case upon the filing of the bill and answer, the court appointed only a temporary receiver on October 2, 1923, directing that notice be given to creditors for the purpose of determining whether the receivership should be continued (R., p. 19). The bill of complaint alleged that if the assets of the defendant could be liquidated in the usual and ordinary course of defendant's business, its assets would largely exceed its lawful obligations; that its quick assets nearly equalled its liabilities and that in addition it had slow assets of approximately $1,000,000. The temporary receiver was continued from time to time until January, 1924, when the receivership was made permanent (R., p. 19). In the intervening period, attempts at reorganization were made but these failed, and finally

the sale of the assets was directed (R., p. 6). The general creditors will receive between 30% and 40% of the amount of their respective claims (R., p. 7).

Pursuant to an order for the filing of claims, the United States of America filed a claim for additional income taxes for the year 1920 and also a claim for additional duties on importations made by the defendant before the receivership (R., p. 7). The details of these claims are accurately set forth in the Master's report (R., p. 1). The claim for taxes, as finally reduced, amounted to the sum of $15,112.47. There was an overpayment by the receiver of taxes for the year 1923, the details of which appear in the said report of the Master. From that report it is apparent that if the Government's claim for taxes is entitled to priority, it is to be allowed at the sum of $11,331.07, and that if it is not entitled to priority, it is to be allowed as a general claim at $14,480.98 and that no dividends are to be paid thereon until the receiver has been recouped for the full amount of the over-payment made by him, to wit, the sum of $3,149.91 (R., p. 3).

Applicable Provisions of the Constitution and of the Revised Statutes.

The Constitution.

The Constitution, Article 1, provides:

> "SECTION 1.—All Legislative powers herein granted shall be vested in a Congress of the United States which shall consist of a Senate and House of Representatives."

Article 1, Section 8 of the Constitution provides:

> "The Congress shall have power to lay and collect *taxes*, duties, imposts and excises, to pay the *debts* and provide for the common defense and general welfare of the United States; but all duties, imposts and excises shall be uniform throughout the United States."

The Constitution, Article 1, Section 8, Clause 18, provides that Congress shall have power:

> "To make all laws which shall be necessary and proper for carrying into execution the foregoing powers and all other powers vested by this Constitution in the Government of the United States or in any Department or officer thereof."

Revised Statutes.

Section 3466 of the Revised Statutes (Compiled Statutes 1916, Section 6372) provides as follows:

> "Priority established. Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority hereby established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed."

Section 3467 of the Revised Statutes (Compiled Statutes 1916, Section 6373) provides:

> "*Liability of executors, etc.*
>
> "Every executor, administrator, or assignee, or other person, who pays any debt due by the person or estate from whom or for which he acts, before he satisfies and pays the debts due to the United States from such person or estate, shall become answerable in his own person and estate for the debts so due to the United States, or for so much thereof as may remain due and unpaid."

Section 3186 of the Revised Statutes (Compiled Stat., Section 5908), provides as follows:

"If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount shall be a lien in favor of the United States from the time when the assessment list was received by the collector, except when otherwise provided, until paid, with the interest, penalties, and costs that may accrue in addition thereto upon all property and rights to property belonging to such person; Provided, however, that such lien shall not be valid as against any mortgagee, purchaser, or judgment creditor until notice of such lien shall be filed by the collector in the office of the clerk of the District Court of the District within which the property subject to such lien is situated; Provided, further, whenever any State by appropriate legislation authorizes the filing of such notice in the office of the registrar or recorder of deeds of the Counties of that State, or in the State of Louisiana in the parishes thereof, then such lien shall not be valid in that State as against any mortgagee, purchaser, or judgment creditor, until such notice shall be filed in the office of the registrar or recorder of deeds of the county or counties, or parish or parishes in the State of Louisiana, within which the property subject to the lien is situated."

Errors Relied Upon.

The errors relied upon are:

(1) That the court below erred in affirming the order of the District Court, affirming the report of the Special Master allowing the claim of the United States as a priority claim.

(2) That the court below erred in holding that the United States of America was entitled to prority in payment of its claim over the claim of general creditors of the defendant corporation.

Brief of Argument.

The petitioner contends:

(1)

At common law the Crown of Great Britain by virtue of prerogative right had a priority over all subjects for the payment out of a debtor's property of all claims due it, whether for ordinary debts or taxes. This prerogative right was based in both instances upon the principle that where the rights of the crown and a subject against a common debtor concurred, the rights of the Crown prevailed. In some states it has been held that this right devolved upon the people of the state and in other states the contrary conclusion has been reached.

(2)

The Federal Government never adopted the common law as the foundation of its jurisprudence and has no inherent sovereign right of priority for the payment of taxes or of ordinary debts. The decisions of this court from the earliest times are to the effect that the federal government did not inherit the prerogative right of the crown of England for the prior payment of debts and that the right of the United States to assert priority must be found in Federal statutes passed by Congress in the exercise of its delegated powers to pass all laws necessary to give effect to the express delegated power to pay debts.

(3)

The distinction between the nature of an obligation *ex contractu* and the obligation to pay a tax is immaterial to the question presented, in the light of the history and purpose of sovereign priority and in the light of the relationship between the people of the states and the Federal Government.

As the priority of the Federal Government for a debt depends upon the exercise of the delegated power to pass all laws necessary for carrying into execution the

express power *to pay debts*, so too the priority of the Federal Government for a tax must also depend upon the exercise of a like delegated power to pass all laws necessary for carrying into execution the express power *to levy and collect taxes and duties.*

(4)

Congress from the earliest times has recognized that the Federal Government has no sovereign right of priority with respect to the prior payment of any claim, and such priority was created, and executors and other trustees were made liable for a failure to recognize it, in the early revenue statutes which subsequently became Sections 3466, 3467 of the Revised Statutes. The history of those sections shows that they primarily were intended to secure a priority for public revenues *and those sections measure the priority for taxes.*

(5)

Section 3466 does not create a priority for ordinary debts or for taxes where the assets of a corporation are distributed in a judgment creditor's suit or equity receivership.

(6)

Congress has by the Revised Statutes provided a comprehensive method for the collection of taxes and has provided for a lien and distraint, and as the provisions of Revised Statutes 3186 *et seq.* as amended in 1913 were not complied with in this case prior to the receivership, a tax claim is not entitled to priority.

(7)

The Federal officials charged with the duty of collecting the internal revenue have always practically construed Sections 3466 and 3467 to include claims for taxes

and have heretofore always asserted the right to priority and the right to hold executors and trustees personally liable, solely because of the provisions of those sections.

The proof of claim in this very case bases the right of priority and the alleged obligation of the receiver upon the provisions of the Statute. This practical construction should not be disturbed, except for very cogent reasons.

POINT I.

At common law the crown of Great Britain by virtue of prerogative right had a priority over all subjects for the payment out of a debtor's property of all claims due it, whether for ordinary debts or taxes. This prerogative right was based in both instances upon the principle that where the rights of the crown and a subject against a common debtor concurred, the rights of the crown prevailed.

In some states it has been held that this right devolved upon the people of the state and in other states the contrary conclusion has been reached.

At common law, the right of the crown to the prior payment of obligations due it, whether such obligations were ordinary debts or duties or taxes, was predicated upon two distinct prerogatives. The *first*, that the crown was not bound by a statute, in which it is not specially mentioned and therefore might pursue its remedies under winding-up statutes which did not specifically refer to the crown's rights, and the *second*, that when the rights of the crown and of a subject against a common debtor concurred, the rights of the crown prevailed. Authorities both in England and in this country recognize no distinction in these prerogatives between claims arising

out of contractual obligations or out of unpaid taxes or other civil obligations. Both kinds of obligations are termed "debts." The leading English cases are the following:

Giles vs. *Grover*, 9 Bing. 128;
In re Henley & Co., 9 Chancery Div. 469;
Commissioners of Taxation for the State of New South Wales vs. *Palmer*, 1907 Appeal cases 179;
In re Webb & Co., L. R. 1922, Ch. Div. 369.

In this country some of the states have held that the principle of the common law with respect to sovereign priority has devolved upon the people of the state as an inherent right, whereas in other states it is denied that the common law principle has so devolved.

See collection of cases in *Equitable Trust Co.* vs. *Connecticut Brass Co.*, 290 Fed., 712, at 716.

One of the best statements of the English procedure is found in *Middlesex County* vs. *State Bank*, 29 N. J. Eq. 268, aff'd on opinion below, 30 N. J. Eq. 311.

The same historical facts may be found in the following cases:

State of Maryland vs. *The Bank*, 6 Gill & J., 205;
Matter of Devlin, 180 Fed., 170, 174, and cases cited.

In *Marshall* vs. *New York*, 254 U. S., 380, the case involving the priority of the State of New York *for taxes*, this court, in considering the nature of the crown's prerogative right for the prior payment of its taxes, considered them to be in the same category as debts, for this court said at page 382:

> "At common law the crown of Great Britain, by virtue of a prerogative right, had priority

> over all subjects for the payment out of a debtor's property of all debts due it. The priority was effective alike whether the property remained in the hands of the debtor, or had been placed in the possession of a third person, or was in *custodia legi*. The priority could be defeated or postponed only through the passing of title to the debtor's property, absolutely or by way of lien, before the sovereign sought to enforce his right. *Giles* vs. *Grover*, 9 Bing. 128, 139, 157, 183; in *re Henley & Co.*, 9 Ch. D. 469, compare *United States* vs. *National Surety Co.*, decided by this court November 8, 1920, ante, 73."

And in *Matter of Carnegie Trust Company*, 151 App. Div., 606, affirmed 206 N. Y., 390, the New York Court of Appeals, in considering the inherent priority of the State of New York for its claim for *taxes*, held that the sovereign powers of the King, so far as they pertained to civil government, devolved upon the people of the State, and that, therefore, claims or moneys due the King for the support of the Government, whether derived from taxes or other sources, were preferred over the claims of others, and the Court of Appeals further held that this principle of the common law became a part of the common law of the State of New York, in pursuance of its constitutional provisions. The Court of Appeals said:

> "The king, therefore, and the prerogatives that were personal to him being repugnant to our Constitution are abrogated. But his sovereignty, powers, functions and duties, in so far as they pertain to civil government now devolve upon the people of the state and consequently are not in conflict with any of the provisions of our Constitution. In as much, therefore, as the claims or moneys due the king, for the support and maintenance of the government, *whether derived from taxes or other sources of income*, were preferred over the claims of others, it follows that under the first sub-division of the provision of the Con-

> stitution of 1777, quoted, such preference became a part of the common law of our state, and is so continued under our present Constitution."

The English cases above referred to *also* show that the prerogative right for the prior payment of taxes stood upon the same principle as the right for the prior payment of debts.

In *Matter of Henley,* 9 Ch. Div., 467 (1878), a motion was made by Her Majesty's Commissioners for Inland Revenue for a direction to the official liquidator of Henley & Co. to pay out of the assets of the company £56.5s in satisfaction of property and income *taxes* due from the corporation in respect of certain lands—the payment to be made in priority to the other claims against the company. The company was being wound up voluntarily by resolution and the winding up had been continued under the supervision of the court. The court held that the crown was not bound by the Winding Up Act and therefore could have issued its writ of extent, but it held further that this was not necessary and that the claim could be made by the Liquidator because of the crown's prerogative right to be preferred when its claim concurred with that of other creditors. Several opinions were written. BRETT, L. J., said:

> "There are two prerogatives of the crown bearing upon this question. The first is that the crown is not bound by a statute in which it is not specially mentioned. Therefore the crown is not bound by the Companies Act. It follows that **this being clearly a debt** for which the crown can distrain, its power of distress is not taken away by the Act, and it can proceed to distrain in this case. It is, therefore, right that the **debt** should be paid in priority to the other creditors.
>
> "But suppose we regard it merely as a simple contract debt; then in the administration of the assets of the company the crown comes into competition with the other simple contract creditors,

and then the other prerogative to which I have alluded comes in, namely, that in competition with subjects, the right of the crown must prevail. Therefore in whichever way we look at the question, I think the crown ought to be paid this debt in priority."

In *Commissioners of Taxation for the State of New South Wales* vs. *Palmer*, 1907, Appeal Cases 179, the question was whether in the administration of the assets of a bankrupt under the New South Wales Bankruptcy Act, the court should have allowed the claim of the crown for land and income *taxes* as a preferential claim. The court below held that as the Bankruptcy Act gave no such priority, the claim was not preferred. The Privy Council of the House of Lords, however, reversed this decision, following the decision in the *Matter of Henley* above referred to, and held that from earliest times the King's debts were to be preferred when his title and that of his subjects concurred. The court said:

"In *Rex* vs. *Wells*, in a passage which has been often cited, MACDONALD, C. B., says: 'I take it to be an incontrovertible rule of law that where the King's and the subject's title concur the King's shall be preferred.' Except so far the Legislature has thought fit to interfere, the rule is one of universal application, and perhaps not unreasonably, when it is considered that, after all, it *only means that the interests of individuals are to be postponed to the interests of the community.* The rule is enunciated by Lord COKE in *Quick's* case. From Lord Coke's time to the present day it has never been questioned as a rule of law, and, so far as their Lordships are aware, there has never been any attempt on the part of any Court to limit the generality of its application except in the present case, and in two recent cases in the Colonies which will be referred to presently.

* * * * * *

It can hardly be disputed that in the present case the rights of the Crown and the rights of

ordinary creditors or 'common persons' (as the phrase is in the old cases) do concur or come into competition. It is admitted that the Bankruptcy Act., 1898, does not bind the Crown. It would therefore seem, on principle, that in the administration of the assets under the direction of the Court it was the duty of the Court to give effect to the Crown's prerogative.

As regards authority both in England and Ireland, the highest Courts in the country, short of the House of Lords, have upheld the prerogative of the Crown. The judgment of the Court of Appeals in *In re Henley & Co.* seems to their Lordships, as it did to SIMPSON, *J.*, to be clear upon the point. The decision was rested upon two separate grounds and upon two distinct prerogatives. It was a case of winding up, not of bankruptcy. The property had not passed out of the Company. The Court therefore held that the Crown was still at liberty to pursue its extreme rights against the Company's property and was on that ground entitled to priority. But the Court also held that under the other and wider prerogative the claim of the Crown must prevail. 'If the matter,' said JAMES, *L. J.*, 'is treated as a matter solely of administration of assets under the direction of the Court I think it is also right. Whenever the right of the Crown and the right of a subject with respect to the payment of a debt of equal degree come into competition, the Crown's right prevails. Whether, therefore, the **debt** is treated as a debt of record or of specialty or of simple contract, there being a right of priority in the Crown, it is right that the debts should be paid.'

* * * * * *

The attention of their Lordships was called to the case of *In Re Baynes*, which has already been mentioned, and a case in Ontario, *Clarkson* vs. *Attorney-General of Canada*, in both of which the right of the Crown to preferential payment out of assets being administered in bankruptcy was denied. Their Lordships have carefully considered those cases. With every respect to the Courts

> by which they were decided, their Lordships cannot help thinking that in both cases the learned judges have not sufficiently kept distinct the two prerogatives which formed separate grounds of decision in *In Re Henley & Co.* The judgments are devoted in a great measure to a consideration of the prerogative under which the Crown was entitled to peculiar remedies against the debtor and his property, and of the law and the authorities bearing upon it. The principle upon which that prerogative depends is not to be confounded with the principle invoked in the present case. The prerogative, the benefit of which the Crown is now claiming, depends, as explained by MACDONALD, *C. B.*, in *The King* vs. *Wells*, upon a principle 'perfectly distinct * * * and far more general, determining a preference in favor of the Crown in all cases and touching all rights of what kindsoever where the Crown's and the subject's right concur and so come into competition ' "

In *Matter of Webb*, L. R., 1922, Ch. Div., 276, the Court of Appeal expressed some doubt as to whether there were really two prerogatives as indicated in the foregoing cases and seemed to believe that the better view was that there was one prerogative, but two methods of enforcement.

Conclusions from Foregoing Authorities.

The foregoing authorities make it clear that the prerogative right of the crown of priority *parens patriae* for taxes and for all other forms of obligations to the crown are based upon the principle that where the rights of the crown and a subject against a common debtor concur, the rights of the crown prevailed. And it is further apparent that this rule of the common law was based upon the further principle that the interests of the individuals were to be postponed to the interests of the community. It also has been made to appear that in some of the states it has been held that these principles of the

common law devolved upon the people of the state, and that in others, just the contrary conclusion has been reached.

It now will be shown that the Federal Government has never adopted the common law principle and that from the earliest times, this court has held that the Federal Government, as distinguished from the people of the states, did not inherit the prerogative right of the crown for the prior payment of debts, and that the right of the United States to assert a priority must be found in statutes passed by Congress in the exercise of its delegated powers.

POINT II.

The Federal Government never adopted the common law as the foundation of its jurisprudence and has no inherent sovereign right of priority for the payment of taxes or of ordinary debts. The decisions of this Court from the earliest times are to the effect that the Federal Government did not inherit the prerogative right of the crown of England for the prior payment of debts and that the right of the United States to assert a priority must be found in Federal Statutes passed by Congress in the exercise of its delegated powers to pass all laws necessary to give effect to the express delegated power to pay debts.

As will be shown at greater length hereafter, by statutes passed in 1789, 1792 and 1797, immediately following the adoption of the Constitution Congress recognized the absence of *sovereign* prerogative right of priority and Congress passed acts *creating* priority, in the event

of insolvency of a debtor, *first* upon bonds given for customs duties, and bonds given by revenue agents, and later by the Act of 1797 upon indebtedness arising upon a bond "or otherwise."

In 1801, both the scope of these statutes and their constitutionality were before this court in *United States* vs. *Fisher*, 2 Cranch 358. This court held that the words "or otherwise" in the Act of 1797 extended the priority to all forms of indebtedness. The court also upheld the constitutionality of the Act of 1797, upon the ground that the preference claimed by the United States was not prohibited by the Constitution; that by the constitution Congress was granted the power "to pay the debts," and was also given the power to make all laws necessary and proper for the carrying into execution the foregoing power, and that, accordingly, in the exercise of its delegated powers, Congress had the right to provide a means which appears most eligible to carry out the express powers. This court, speaking through Chief Justice Marshall, said:

> "If the act has attempted to give the United States a preference in the case before the court, it remains to inquire, whether the constitution obstructs its operation. To the general observations made on this subject, it will only be observed, that as the court can never be unmindful of the solemn duty imposed on the judicial department, when a claim is supported by an act which conflicts with the constitution, so the court can never be unmindful of its duty to obey laws which are authorized by that instrument. In the case at bar, the preference claimed by the United States is not prohibited; *but it has been truly said, that under a constitution conferring specific powers, the power contended for must be granted, or it cannot be exercised.* It is claimed, under the authority to make all laws which shall be necessary and proper to carry into execution the powers vested by the constitution in the government of the United States, or in any department or officer thereof. In construing this clause, it would be incorrect, and

> would produce endless difficulties, if the opinion should be maintained, that no law was authorized which was not indispensably necessary to give effect to a specified power. Where various systems might be adopted for that purpose, it might be said, with respect to each, that it was not necessary, because the end might be obtained by other means. Congress must possess the choice of means, and must be empowered to use any means which are in fact conducive to the exercise of a power granted by the constitution. *The government is to pay the debt of the Union, and must be authorized to use the means which appear to itself most eligible to effect that object.*"*

Since that decision, it has been the uniform holding of this court that the right of priority of the United States does not stand upon any sovereign prerogative, but is exclusively founded upon the provisions of the statute. In *United States* vs. *Bank of North Carolina*, 6 Peters, 29, 35, this court said:

> "The right of priority of payment of debts due to the Government is a prerogative of the crown well known to common law. It is founded not so much upon any personal advantage to the sovereign, as upon motives of public policy, in order to secure an adequate revenue to sustain the public burdens, and discharge the public debts. The claim of the United States, however, does not stand upon any sovereign prerogative, but is exclusively founded upon the actual provisions of their own statutes. The same policy which governed in the case of the royal prerogative, may be clearly traced in these statutes: and as that policy has mainly a reference to the public good, there is no reason for giving to them a strict and narrow interpretation. Like all other statutes of this nature, they ought to receive a fair and reasonable interpretation, according to the just import of their terms."

*The principle that Congress had the right to use the means which it found necessary or expedient to exercise its express power was of course more elaborately considered in the later case of *McCulloch* vs. *Maryland*.

In *United States* vs. *Canal Bank*, 3 Story, 79, Federal case #14,715, Judge STORY, sitting in the Circuit Court, thus summed up the prior decisions of this court:

> "It has long since been settled, by the solemn adjudications of the supreme court, that the United States do not possess any general right of priority or privilege over private creditors, for the satisfaction of the debts due to them, founded upon any general prerogative, belonging to the government in its sovereign capacity; but that all the priority or privilege, which the government is at liberty to assert, is or must be founded upon some statute, passed by Congress, in virtue of its constitutional authority. This was expressly so held in *U. S.* vs. *Fisher*, 2 Cranch (6 U. S.), 358, 396, and the doctrine has ever since been strictly adhered to. *U. S.* vs. *Hooe*, 3 Cranch (7 U. S.), 73; *Prince* vs. *Bartlett*, 8 Cranch (12 U. S.), 431; *Thelleson* vs. *Smith*, 2 Wheat. (15 U. S.), 396; *U. S.* vs. *Howland*, 4 Wheat. (17 U. S.), 108; *Conrad* vs. *Atlantic Ins. Co.*, 1 Pet. (26 U. S.), 387. It is not here, as it is in England, where the sovereign is entitled, in virtue of his prerogative, to a priority over private creditors, for satisfaction of the debts due to the crown. Com. Dig., 'Prerogative,' D. 86; id. 'Debt,' G. 8, G. 9."

The latest exposition of these principles is found in *United States* vs. *Oklahoma*, 261 U. S., 253.

Thus it appears that the principle is established that while the common law sovereign right of priority devolved in some states upon the people of the state, that this principle of the common law and this sovereign right did *not* devolve upon the Federal Government and that any claim of the latter for priority over the claims of ordinary citizens was founded solely upon statutes passed by Congress in the exercise of its delegated powers.

It is, of course, true that in none of the foregoing Federal cases was a claim for taxes or duties, as such, in-

volved, and because of this fact and because of an asserted distinction between taxes and ordinary debts, it has been held below that the Federal Government has inherited an inherent sovereign prerogative right of priority for the payments of its *taxes*, when its claim comes into competition with the claim of the ordinary citizen.

It now will be shown that there is no basis for this distinction.

POINT III.

The distinction between the nature of an obligation ex contractu and the obligation to pay a tax is immaterial to the question presented, in the light of the history and purpose of sovereign priority and in the light of the relationship between the people of the States and the Federal Government.

As the priority of the Federal Government for a debt depends upon the exercise of the delegated powers to pass all laws necessary for carrying into execution the express power to pay debts, so too the priority of the Federal Government for a tax must also depend upon the exercise of a like delegated power to pass all laws necessary for carrying into execution the express power to levy and collect taxes and duties.

It is, of course, conceded that the nature of an obligation arising *ex contractu* is different from that arising from the payment of a tax. In the language of this court in *Guarantee Title & Trust Co.* vs. *Title Guaranty & Surety Co.*, 224 U. S. 152, the one is a "personal convention" and the other a "civil obligation." Such a civil obligation is no doubt a *quasi* contractual obliga-

tion. But this distinction while important for many purposes, and in the construction of certain statutes is not deemed important or decisive of the question presented here.

As has just been shown, in all the authorities both in England and here, the priority of the crown and of the states for taxes and for debts rested on precisely the same principle, namely, that when the right of the sovereign or of the state and those of a subject or a citizen against a common debtor concurred, the sovereign or the state was to be preferred, so as to insure the public revenue. Whether those public revenues have their source in a *bond* given for the payment of duties as a conditions of the release of imported merchandise or have their source in an obligation to pay such duties or pay income or other taxes, can be of no importance. If the Federal Government, as has been held since 1801, has no sovereign priority for the prior payment of an obligation arising upon a bond for duties because the common law principle has not been inherited by the Federal Government and that Government as one of delegated powers must create a priority, then the same rule must obtain with respect to a claim for taxes, and a holding to the contrary must over-rule all the cases from *United States* vs. *Fisher* to *United States* vs. *Oklahoma*.

Article 1, Section 8 of the Constitution, grants to Congress *both* the power to lay and collect taxes and to pay the debts. The power to lay and collect taxes granted to Congress is no less a delegated power than a power to pay debts. Both are to be sure sovereign powers which inhere in the people, but it is the people who have delegated to the Federal Congress certain legislative powers, for, as stated in Article 1, Section 1 of the Constitution,

> "Legislative powers herein granted shall be vested in the Congress of the United States."

Thus the people have delegated to the Federal Congress

both the power to tax and to pay debts. Whether, therefore, Congress creates a priority to make effective its express power to provide for the payment of the debts of the Union (*U. S.* vs. *Fisher, supra*), or to make effective its express power to lay and collect taxes, is immaterial. The creation of a priority in either case is for the protection of public revenues. In either case the priority is a creation of statute passed in pursuance of the power vested in Congress under Section 8, Clause 18, namely, the power to make all laws necessary and proper for carrying into execution the express powers vested in Congress by the Constitution.

The court below laid stress upon the language of this court in *United States* vs. *Bennett*, 232 U. S., 299, 306 and *Cook* vs. *Taite*, 265 U. S., 47. The Court below said:

> "In *United States* vs. *Bennett*, 232 U. S., 299, 306, Chief Justice WHITE, alluding to the limitations upon the power of the States to tax, says that they afford no ground for constructing an imaginary constitutional barrier around the exterior confines of the United States 'for the purpose of shutting that government off from the exertion of powers which inherently belong to it by virtue of its sovereignty.' "

But those cases, of course, were considering the *extent* of the *power* of Congress to tax and not the question whether Congress had *exercised* that power or any other power. They simply held what this court many times before had already held, namely, that the power of taxation granted by the people to Congress by the Constitution is in its very nature a sovereign power although delegated, and has no limitations, except those stated in the Constitution, and is, in fact, *co-extensive* with that of a sovereign power.

In *Dobbins* vs. *Erie County*, 16 *Peters*, 434, 446, Justice WAYNE said in discussing the taxing power of the State and of the Federal government:

> "Both are restrained upon this subject, by express prohibitions in the constitution; and the states, by such as are necessarily implied, when the exercise of the right by a state conflicts *with the perfect execution of another sovereign power, delegated to the United States;* that occurs when taxation by a state acts upon the instruments, emoluments and persons which the Untied States may use and employ as necessary and proper means to execute their sovereign powers. The government of the United States is supreme within its sphere of action. The means necessary and proper to carry into effect the powers in the consitution, are in congress. Taxation is a sovereign power in a state; but the collection of revenue by imposts upon imported goods, and the regulation of commerce are also sovereign powers in the United States."

To same effect,

> *Collector* vs. *Day*, 11 Wall, 113;
> *McCulloch* vs. *Maryland*, 4 Wheat., 315, 433.

In *McCray* vs. *United States*, 195 U. S., 27, 61, Mr. Justice WHITE says:

> "The right of Congress to tax *within its delegated power being unrestrained*, except as limited by the Constitution, it was within the authority conferred on Congress to select the objects upon which an excise should be laid."

In *Martin* vs. *Hunter*, 1 Wheat., 304, 326, this Court says:

> "The government, then, of the United States can claim no powers which are not granted to it by the constitution, and the powers actually granted, must be such as are expressly given, or given by necessary implication."

The two cases referred to in the Court below cannot be

construed to hold that the Federal power of taxation is a power which would exist *independent of any constitutional grant,* and for that reason there would attach to it the sovereign right of priority of the British crown. It was largely the absence of the taxing power under the articles of Confederation that required the adoption of the Constitution. If the Federal Government has an inherent power to tax as a sovereign government, then it has a like power to pay its debts, and the inherent priority, if it exists in the one case, must exist in the other.

The power of Congress to *create* a priority is conceded. That Congress has exercised that power by Section 3466 of the Revised Statutes, where a debtor has been divested of his property by bankruptcy or general assignment, is conceded, but that such power has been exercised by Congress where a debtor's property is disposed of by judgment creditor's bill or by equity receivership, is denied. (See Point V, *infra*). Whether or not there should be such a priority in such a case is a legislative and not a judicial question.

Even if this court should believe that such a priority should exist, as stated by this Court in *Ebert* vs. *Postom,* 69 L. Ed., 215, 217:

> "A *casus omissus* does not justify judicial legislation."

The Dictum in the Dollar Savings Bank Case Inapplicable.

The decision below is largely based upon the dictum in the *Dollar Savings Bank* case, 19 Wallace, 227, 239, that so much of the royal prerogative as belonged to the King in his capacity as *parens patriae* or universal trustee, is as much a part of the national government as it is a part of the British constitution. Of course, if this dictum is sound, in so far as it applies to the sovereign

right of priority, then under our political system the conclusion must be inevitable, that the King's prerogative for the payment of *ordinary debts* is also a part of the national government and the decisions for a period of 100 years have erroneously denied the United States its priority under a variety of circumstances.

It is interesting to note that in *Equitable Trust Co.* vs. *Connecticut Brass*, 290 Fed., 712, the same Circuit Court of Appeals as decided the case at bar, held that the dictum was inapplicable when a priority was asserted for an ordinary debt. For in holding inapplicable the dictum of the *Dollar Savings Bank* case, Judge ROGERS, speaking of that case said:

> "But that case did not involve the question now under consideration, and has never been understood, notwithstanding the generality of the language used, as intended to assert that the United States possesses a right at common law to priority of payment over other creditors. In that case the court was construing a statute which created a right and provided a particular remedy for its enforcement. All that was decided was that such a statute, by impliedly prohibiting other remedies than the one it gave, did not bind the government: it not being named therein."

In *Matter of In Re Burrus*, 136 U. S., 586, the court at page 594 refers with approval to the opinion of Judge Betts in the Circuit Court on the question of the power of the court to exercise the common law function of *parens patriae*, and Judge Betts' opinion is appended to the report of the case. In that opinion at 136 U. S., p. 604, is an elaborate discussion of the subject. Judge BETTS there says:

> "Does this common law prerogative, in relation to infants, rest in the government of the United States, and has the Circuit Court competent authority to exercise it?
>
> "The argument bearing upon the first branch

of this inquiry assumes two propositions as its basis: (1), that the government of the United States is supreme over all subjects within its cognizance; and (2) that the common law of England is embodied with, and has become a measure and source of authority to, the national government, and is to be enforced in the Circuit Court, whenever persons competent to sue in those courts prosecute their rights therein. It is believed that neither of these propositions can be maintained, and certainly not in respect to the subject matter of this proceeding.

"Many of the powers of the general government are unquestionably supreme and exclusive, while others, especially those in relation to remedies afforded by its courts to private suitors, are only concurrent with similar powers possessed by the state governments. If the power in respect to parties competent to sue in the national federal courts could be supposed to exist in its absolute sense in the United States Government, its exercise has been modified and restricted by Congress in the 11th section of the act of September 24, 1789, which gives the Circuit Courts no more than a concurrent jurisdiction with the state courts, of suits of a civil nature, at common law. 2 Stat., 60.

"Nor again do all attributes of sovereignty devolve upon the national government. Whether considered as emanating directly from the people in their aggregate capacity, or as proceeding from the States, in their independent organization and character, the government of the Union is one of special powers, defined or necessarily implied in the terms of the grant. *McCullough* vs. *Maryland*, 4 Wheat., 407; 2 Story Const., Sec. 1907; *Rhode Island* vs. *Massachusetts*, 12 Pet., 657.

"Though the point has been labored with ability by a late jurist of eminence in this department of legal learning, to deduce from the circumstances attendant upon the establishment of this government, that the common law became embodied in it, as an efficient principle of its authority and action, (Du Ponceau on Jurisd., 85-90),

yet the doctrine has never been declared or sanctioned by our courts.

"So far as the decisions have gone, they tend to repudiate the principle *in toto*. *United States* vs. *Hudson*, 7 Cranch., 32; *United States* vs. *Coolidge*, 1 Wheat., 415.

"There is, accordingly, no sure foundation for the assumption that the federal government possesses common law prerogatives inherent in the sovereign, which can be exercised without authority of positive law. *Martin* vs. *Hunter*, 1 Wheat., 304, 329.

"If any common law prerogative in relation to the administration of justice can be proved to exist in the sovereignty of the United States, it must, upon the same principle, be endowed with all such prerogatives, and can, on the like authority, unless inhibited by positive law, award writs of mandamus, *quo warranto*, *ne exeat*, or mandates to citizens abroad to return home on pain of confiscation of their estates (Comyn's Dig. Prerogatives, D. 34, 35), or this writ of *habeas corpus;* they being all common law writs *ejusdem generis*.

"That such attributes or functions of sovereignty cannot be inherent in the United States government necessarily results from the character of the government and the objects of its constitution."

It is submitted, therefore, that the dictum in the *Dollar Savings Bank* case has no application to the question of sovereign priority.

And yet, in the present case, in its essence, the decision below is based upon this very dictum.

It is not apparent that there is anything in the nature of the prerogative right of sovereign priority which justifies the holding that the right of the King parens patriae devolved upon the Federal Government when a tax claim was asserted, but did not devolve when the claim was for a bond for duties.

It is to be noted in the *Carnegie Trust* case, 206 N. Y. 397, quoted above, the New York Court of Appeals held

that the right of the King, as Universal trustee, devolved *upon the people of the State,* and that in the court below, 151 App. Div., at 611, Judge Scott said:

> "Of course all the cases dealing with the right of the United States to a preference in payment are beside the mark, for the United States never adopted the common law as a foundation of its jurisprudence, and any right to a preference which it asserts must be found in statutory authority."

Other Alleged Federal Prerogatives Immaterial.

The fact that certain rights, exemptions and immunities of the King of England may now be asserted by the Federal Government, is not persuasive of the existence of a sovereign right of priority for the payment of either debts or taxes.

Thus the rule that neither the Federal nor a state government can be sued without its consent, does not indicate the presence of the sovereign priority. The principle of immunity from suit is based upon wholly different reasons. This immunity, as stated by this court, has been adopted as a part of the general doctrine of publicists, that the supreme power, wherever it may reside, shall not be compelled by process of courts of its own creation, to defend itself of assaults in those courts.

In *United States* vs. *Lee,* 106 U. S., 196, this court found it necessary to ascertain on what principle the exemption of the United States from suit is founded. The court said at page 206:

> "It seems most probable that it has been adopted in our courts as a part of the general doctrine of publicists, that the supreme power in every state, wherever it may reside, shall not be compelled, by process of courts of its own creation, to defend itself from assaults in those courts."

The immunity from the liability for costs stands upon the same principle. So, too, the English doctrine that the King could do no wrong, can have no application to our form of Government. As this court said in *Langford*

vs. *United States,* 101, U. S. 431, in discussing this question:

> "We do not understand that either in reference to the government of the United States, or of the several states, or of any of their officers, the English maxim has an existence in this country."

If the reasoning of the court below is sound that the existence of these rights and immunities of the Federal Government are evidence of the fact that the Federal Government has taken over the prerogative right of priority, then it is hard to understand the reasoning which underlies the conclusion of this court, that such a priority has not been taken over for ordinary debts. Again, if the immunity from suit is persuasive of the existence of the priority, then it is hard to understand why some of the states have denied that the common law principle of priority has been taken over. All states are immune from suit, and yet, some recognize the priority and some do not.

POINT IV.

Congress from the earliest times has recognized that the Federal Government has no sovereign right of priority with respect to the prior payment of any claim, and such priority was created and executors and other trustees were made liable for a failure to recognize it in the early Revenue Statutes, which subsequently became Sections 3466, 3467 of the Revised Statutes. The history of those sections shows that they primarily were intended to secure priority for public revenues and those sections measure the priority for taxes.

The fundamental error of the court below lies in its

holding that a claim for duties or for taxes was not intended to be granted priority by the early revenue acts passed immediately after the formation of the Union, and that this is so, because the words "indebtedness" and "debts," as used in those acts, did not include a claim for duties and taxes, but only claims arising ex contractu. Having reached this erroneous conclusion, the courts concluded that Congress could not have intended that tax claims should have *no* priority, and as no statutory priority was created, there must be found some other method of providing for it, namely, an inherent prerogative right.

Of course even the omission of *any* priority for taxes in the revenue acts is not justification for judicial legislation.

It is believed that an examination of the early statutes, which are now Section 3466 *and* 3467 *of the Revised Statutes, in the light of their underlying purpose, will reveal* (1) *that they were intended by Congress primarily to secure the prior payment of revenue where the debtor was divested of his property in the methods provided and only later were extended to secure prior payment of all obligations to the United States, whatever their nature, and* (2) *were intended to impose a personal liability upon executors and trustees, in the event that the priority was ignored. This conclusion the courts below have refused to adopt, however, because of their narrow interpretation of the words "debts" and "indebtedness."*

Whether revenues are collected through the exaction of a bond or without such bond the purpose of the statute and its scope must be the same. *In either case the Statute measures the extent of the priority.*

As said by this court in *United States* vs. *Chamberlain,* 219 U. S., 250, 262:

"A tax may or may not be a debt under a parti-

cular statute, according to the sense in which the word is found to be used."

The History of Revised Statutes Sections 3466 and 3467.

1. The first priority statute was enacted shortly after the formation of the Union.

The Act of July 31, 1789 (1 Stat., 29), was entitled:

> "An Act to Regulate the collection of the duties imposed by law on the tonnage of ships or vessels and on goods, wares and merchandise imported into the United States."

Section 19 gave the importer the option to give a bond where the duty exceeded $50.00.

Section 21 provided for priority in the following language:

> "And be it further enacted, that where any bond for the payment of the duties shall not be satisfied on the day it became due, the collector shall prosecute for the recovery of the money due thereon, by action or suit at law, and in the proper court, having cognizance therein; and in all cases of insolvency, or where any estate in the hands of executors or administrators shall be insufficient to pay all the debts due from the deceased, the debt due to the United States on any such bonds shall be first satisfied."

2. The next act of importance is the Act of May 2, 1792 (1 Stat., 259). That Act was entitled:

> "An act for raising a farther sum of money for the protection of the frontiers and for other purposes therein mentioned."

The Act levied new duties and by Section 18 sureties on importers' bonds were subrogated to the Government's claim for priority.

3. The next act of importance was the Act of March 3, 1797 (1 Stat., 512). That Act was entitled:

"An Act to provide more effectually for the settlement of accounts between the United States and receivers of public money."

It is the first act to extend the priority to the case of a person other than a revenue officer or obligor upon a custom bond indebted to the United States.

Section 5 of the Act provided:

> "And be it further enacted, that where any revenue officer, *or other person* hereafter becoming indebted to the United States, by bond or *otherwise*, shall become insolvent, or where the estate of any deceased debtor, in the hands of executors or administrators, shall be insufficient to pay all the debts due to the United States shall be first satisfied; and the priority hereby established shall be deemed to extend, as well to cases in which a debtor not having sufficient property to pay all his debts, shall make a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed or absent debtor, shall be attached by process of law, as to cases in which an act of legal bankruptcy shall be committed."

4. The next Act of importance is the Act of March 2, 1799.* This act was entitled "The Act to Regulate the Collection of Duties on import and tonnage," provided for revenue districts and prescribed the duties of collectors. Provision is made for priority upon bonds for the subrogation of sureties, and in addition, there is here found *for the first time*, the provisions for personal liability of executors and assignees which later became Section 3467 of the Revised Statutes.

Conclusions from Foregoing Acts.

From the foregoing acts, it is apparent that there were three classes of debtors of the United States:

(1) Debtors on credit for public dues, that is for import duties or for internal taxes;

*1 Stat., pp. 627, 676.

(2) Government officials who received public money, that is, revenue officers;

(3) Debtors on ordinary contractual or commercial transactions with the Government.

By the first act passed in 1789, priority was created for revenues accruing on bonds for duties. By the Act of 1792, a like priority was given to the sureties upon such bonds. Thus, as early as 1792, priority in the case of bonds for duties on imported merchandise was complete. As early as 1791 (1 Stat., 203), taxes were imposed on distilled spirits, which were to be secured by bond, and in 1794 (1 Stat., 387), duties were imposed on snuff and sugar, likewise to be secured by bond. No priority, however, was created by those acts to insure the collection of these duties. The collection of internal revenues was essential to the government at a time when foreign war was threatened, and, accordingly, in 1797 the Act of March 3rd, 1797, was passed (1 Stat., 505). That act provided that where any revenue officer or other person "hereafter became indebted to the United States by bond *or otherwise*," and such person was insolvent, the debt due the United States should first be satisfied, etc.

And by the Act of March 2, 1799, the priority was repeated and an additional provision made that every executor, administrator, assignee or other person who pays any debt due by the person or estate from whom or for which he acts, before satisfying debts due to the United States, should be personally liable therefor.

The construction of these Acts was first before this court in *United States* vs. *Fisher*, 2 Cranch., 358, and this court reached the conclusion that by the Act of 1797, through the use of the words "indebted upon a bond *or otherwise*," it was intended to grant a priority to the United States, upon any form of indebtedness which might arise, and that the priority was not *limited* to

claims upon revenue bonds or against revenue collectors. After pointing out the limitations in the earlier Acts, Chief Justice MARSHALL said at p. 392:

> "Such was the title of the United States to a preference in the payment of debts, previous to the passage of the act of 1797. It was limited to bonds for the payment of duties on *imported* goods, and on the tonnage of vessels. An *internal* revenue had been established, and extensive transactions had taken place; in the course of which, many persons had necessarily become indebted to the United States. But no attempt to give them a preference in the collection of such debts had been made."

Having in mind the purpose of these statutes, namely, assurance of the collection of internal revenue of the United States, it is hard to understand why the statute should be given a narrow construction. Not only did Congress provide for the priority in the Act of 1797, but so anxious was it to protect the revenue, that in the Act of 1799 it provided a personal liability upon the executor or other trustee, who failed to recognize the Government's priority.*

Absurd Result Flowing from Government's Contions.

If the argument of the Government in the present case is sound and these statutes were *not* intended to include income taxes and duties, because they are not secured by bond, then it must follow, of necessity, under the Provisions of the Act of 1799, now Section 3467 of the Revised Statutes, that an executor or assignee or other trustee who pays private debts of a *cestui* before he pays contractual *debts* due the United States, is *liable* for the amount remaining unpaid. But if he pays such private

*It also shows that *duties* as such and not merely bonds were within the purview of the act, for it provides: "That in all cases in which suits * * * shall be commenced for the *recovery of duties* * * * the person * * * may be held to special bail.

debts before paying *taxes* due the United States, there is *no* such personal liability, because none is provided for in the statute. That is, the result must be that there is no penalty for ignoring the higher form of obligation to the United States.

It is, of course, true that at the time of the enactment of these Revenue Acts and the provisions for the insuring of the collection of the internal revenue, that there was no income tax payable and that income taxes, apportioned between the states, were not passed until some later period. But if the underlying purpose of the Revenue Acts passed in 1797 and 1799 was to secure a priority first for revenues and finally for the indebtedness due from all persons, whether upon bond "or otherwise," then the mere fact that the internal revenue today is collected by direct tax, rather than by a bond evidencing indirect taxation, cannot result in the conclusion that the primary purpose of Congress in the enactment of these statutes, was not to grant a priority for internal revenue, however, it was imposed,—whether the obligation accrued out of the exaction of a bond or a quasi contractual debt, the duty of the citizen to pay.

The foregoing views find support in the decisions of this court.

In construing the early statutes, this court said in *United States* vs. *Bank of North Carolina*, 6 Peters, 29, 35:

> "The same policy which governed in the case of the royal prerogative, may be clearly traced in these statutes; and as that policy has mainly a reference to the public good, there is no reason for giving to them a strict and narrow interpretation. Like all other statutes of this nature, they ought to receive a fair and reasonable interpretation, according to the just import of their terms."

It already has been shown that the royal prerogative was for taxes and for debts, and if the statute, as stated by this court, is not to have a narrow and strict construc-

tion, it is hard to see why, according to the "just import" of its terms, it can be said that the intention was not to include all forms of obligations to the Government. The limitations which this court has placed upon the statute, as hereinafter shown, are not upon the form of indebtedness which is entitled to priority, but upon the method by which the debtor has been divested of the control of the property and by which the property is distributed amongst his creditors.

The English cases, quoted above, clearly indicate that in construing the crown's inherent prerogative, the courts considered a tax to be a debt in the broad sense of the term and no different construction should be given to the statute in this country, which creates a priority where the debtor is divested of his property in certain specific ways. In other words, in those specific cases priority created by the statute is co-extensive with the inherent prerogative of the crown.

It is interesting to note that under the Bankruptcy Act of 1898, which grants a specific priority for taxes and grants no priority for ordinary debts due the United States (*Davis* vs. *Pringle*, decided in this court May 25, 1924), taxes are deemed to be debts for the purposes of determining whether sufficient amount of indebtedness exists to put the debtor into bankruptcy.

Kaw Boiler Works vs. *Schull*, 230 Fed., 587.

In State ex rel. vs. *Mississippi Valley Trust Co.*, 209 Mo., 472, the court, in a very able opinion, held that while it was not necessary to determine in that case whether taxes are technically a debt or not, they might properly be treated as such, for the purpose of allowance against the estates of deceased persons and for classification.

In *United States* vs. *Chamberlain*, 219 U. S. 250, it was held that an action in debt would lie to recover the amount of a stamp tax payable under the Revenue Act of 1898.

In *Miller* vs. *Robertson*, 69 L. Ed. 54, decided November 17, 1924, this court gave a broad construction to the meaning of the word "debt" in construing the "Trading with the Enemy Act." It held that there was no reason to restrict the word "debt" to a narrow meaning, and this court said at page 57:

> "The meaning of the word 'debt,' as used in many statutes, is not restricted to demands enforceable in the actions of debt. Lord Coke, referring to the Statute of Merten (A. D. 1235) said (Institutes vol. 2, page 89) Debitum signifieth not only debt, for which an action of debt doth lie, but here in this ancient act of Parliament, it signifieth generally any duty to be yielded or paid."

Lane vs. Oregon, and Merriweather vs. Garrett, are not authorities opposed to petitioner's contentions.

Two cases in this court are always cited in support of the conclusion that the words contained in Section 3466

> "whenever any person indebted to the United States is insolvent * * * the debts due the United States shall be first satisfied"

do not include obligations to pay "taxes and duties." These are:

> *Lane* vs. *Oregon*, 7 Wallace 71;
> *Merriweather* vs. *Garrett*, 102 U. S. 472, 513.

But those cases simply construe particular statutes. This court, as a result of such construction, concluded that in those particular statutes, the term "debt" was not intended to include a civil obligation. As stated in this court in the *Chamberlain* case (219 U. S. 250), the text of the statute under consideration in those cases "forbade the conclusion" that Congress intended to include taxes.

In the *Lane* case, a state statute directed the collection of taxes in coin and a federal statute provided that United States notes were receivable in payment of taxes, internal duties, excises, debts and demands due to the United States, and also provided that such notes should be lawful money and legal tender in the payment of all debts, public or private, within the United States. The sole question was whether the latter provision could be deemed to override the provision of the State statute requiring taxes to be paid in coin and whether Congress intended the word debts with reference to the payment of debts generally, to include State taxes. The court held that the power to tax not delegated to the Federal Government remained in the State, and that the taxing power was concurrent and that Congress could not direct the State in what currency its taxes should be collected and that the first clause of the Act, in referring to payments to the United States, *specifically* included taxes, and the second clause, referring to payment of debts generally, did not include taxes.

In *Merriweather* vs. *Garrett*, 102 U. S. 472, suit was brought by the holders of bonds of the City of Memphis, in which it was alleged that despite the fact that the bondholders had procured judgment and mandamus to aid in the collection of the amounts due, a large proportion of taxes which had been levied for prior years, remained uncollected, and in pursuance of certain acts of the Legislature of Tennessee, a receiver was prayed for to take charge of the assets of the city and that he be clothed with power to collect all outstanding indebtedness of every kind due to the city. Prior to the filing of the bill, the charter of the City had been repealed and the territory and inhabitants remanded to the Government of the state. This court held that the relief, insofar as it applied to the collection of taxes through a receiver, could not be granted. The basis for the decision was that taxes levied by authority of the Legislature could be altered, postponed or released at pleasure, and

that a repeal of the law under which a tax was levied, at any time before the tax was collected, put an end to the obligation, and that taxes being merely imposts of government, created and continued only by the will of the Legislature, had none of the elements of property which could be seized for a debt or attachment or other judicial process. (See 102 U. S. 513, 514).

In the course of the opinion, the court pointed out the obvious distinction between debts and taxes which was pertinent to the question before it, which, of course, is not denied, namely, taxes operated in *invitum* and are not founded upon true contract.

These cases have little relevancy to the question as to whether at the end of the eighteenth century, at the inception of this government, Congress intended to provide in insolvency proceedings a priority for all forms of internal revenue due the United States, whether then existing or thereafter imposed, in those particular instances where the debtor was divested of his property, as the statute provided.

In view of the foregoing, it is submitted that it must he held the Revenue Acts of 1797 and 1799, now Sections 3466 and 3467 of the Revised Statutes were intended to create a priority for all forms of internal revenue, whether represented by a bond for duties or imposts, or by a direct obligation to pay the tax imposed by statute, and were intended further to impose a personal liability upon the executor, assignee or other trustee, charged with the duty of the distribution of the insolvent's property, if distribution was made in violation of the provisions of the statute. *Those early statutes measure the extent of Federal priority.*

As pointed out above, if this is not so, then even today an executor, assignee or trustee who pays a private indebtedness of the insolvent before he pays taxes due, is under no personal liability, whereas such personal liability would exist if he failed first to pay ordinary contractual debts due the Federal Government.

It now will be shown, that in the case at bar, the debtor has *not* been divested of its property in any of the methods which the statute prescribes. Therefore, priority created by 3466 is inapplicable.

POINT V.

Section 3466 does not create a priority for ordinary debts or for taxes where the assets of a corporation are distributed in a judgment creditor's suit or equity receivership.

The recent cases in this court of *United States* vs. *Oklahoma,* 261 U. S., 253, and *Strain* vs. *United Fidelity & Guaranty Co.,* 66 L. Ed., 387, which granted a motion to affirm a decision of the Circuit Court of Appeals in 292 Fed., 294, reaffirm the following principles for the construction of Sec. 3466 already laid down in earlier cases:

(1) That section created priority only if the debtor is divested of its property in one of the methods specified in that section, namely, so far as here is applicable, by the making of a general assignment or by "an act in bankruptcy."

(2) That the fact that the debtor cannot pay all his debts in full is immaterial, provided the debtor is not divested of his property, as provided in the statute.

It remains to be shown, therefore, that the judgment creditor's suit or equity receivership did not divest the corporate defendant here of its property in one of the methods prescribed in the Statute.

As to the Nature of the Equity Receivership.

Judgment Creditors' bills are of ancient origin. Their primary purpose was to reach the property of a defendant debtor which could not be reached by the ordinary

process of execution, either because the property was intangible or because it had been transferred in fraud of creditors. The obtaining of a judgment and the exhaustion of legal remedies was a condition precedent to the maintenance of the bill. In the Federal courts, the obtaining of a judgment was necessary because the defendant was entitled to a trial by jury of the fact as to whether or not the indebtedness existed.

Re Metropolitan Ry. Receivership, 208, U. S. 90.

At first, the bill was filed on behalf of a single creditor and he sought to collect only his own indebtedness. Gradually, however, there evolved the procedure of filing a bill under which the rights of all creditors in the property of a corporation were determined, and the property distributed in accordance with the equities of the parties, and finally, it was held that where the defendant corporation admitted the allegation of the bill, it waived its right to trial by jury and waived the defense of an adequate remedy at law, and that, accordingly, under those circumstances, the Federal court of equity would have the right to appoint a receiver.*

The foregoing summary statement of the nature of the present cause finds support in the following cases:

Pa. Steel Co. vs. *N. Y. City Ry.,* 198 Fed. 721, 737;

Pusey Jones Co. vs. *Hanssen,* 261 U. S. 491;

Metropolitan St. Railway, Receivership, 208 U. S. 90;

Luhrig Colleries vs. *Interstate Coal, Etc., Co.,* 281 Fed. 265, affirmed 287 Fed. 711.

In the *Pennsylvania Steel Co.* case, *supra,* Judge Noyes characterizes the proceedings as "equitable levies in favor of all judgment creditors entitled to seize the defendant's property."

*But to sustain Federal jurisdiction the complainant's claim alone must exceed $3,000. *Lion Bonding Co.* vs. *Karatz,* 262 U. S., 77, 86.

The Present Suit is Not the Equivalent of a General Assignment.

In *Davis* vs. *Miller Link Lumber Co.*, 296 Fed. 649, there was a holding that a suit, such as this, was equivalent to a general assignment, and, therefore, that there was a priority in favor of the United States. There is no real basis for this holding. It is, in effect, nothing but judicial legislation. The distinctions between a general assignment and the present suit are obvious. The present suit is nothing but a judgment creditor's action. (*Pusey Jones* case, *supra*). It is a real law suit, with parties plaintiff and defendant. (*Metropolitan Street Railway Receivership, supra*). It is a form of action which was well recognized at the time of the early priority statutes. A general assignment, on the other hand, was also well recognized at that time. It is a voluntary transfer of the property of the debtor in trust for the benefit of his creditors. The debtor is divested of title to his property.

Laclede Bank vs. *Schuler*, 120 U. S. 511.

As said by Judge Lurton in *Vaccaro* vs. *Security Bank*, 103 Fed., 436, 439,

> "A general assignment is the voluntary act of a debtor, whereby he transfers his property to a trustee for the benefit of creditors. Its nature and characteristics were well understood. It is not enough to say that, if the same consequences ensue from the appointment of a receiver, the one act is the equivalent of the other in law."

In *Empire Metallic Bedstead Co.*, 98 Fed., 981, the Court said:

> "It is a deed or conveyance which the grantor makes voluntarily, or sometimes by compulsion, at the instance of a court of insolvency. A petition for the appointment of a receiver is not that proceeding which is universally recognized as an

assignment, and its 'equivalency' of result, if equivalency exists, is not important."

A receiver in equity is a mere custodian, an arm of the court, and takes no title to the corporate property.

Quincey Railroad vs. *Humphreys*, 145 U. S. 82, 98.

An assignee for the benefit of creditors gets title to the property of the assignor, wherever it is situated, and may proceed to collect that property in foreign jurisdictions. An equity receiver has no right to sue beyond the confines of the district for which he is appointed.

Great Western vs. *Harris*, 198 U. S. 561; *Lion Bonding Co.* vs. *Karatz*, 262 U. S. 77.

So strict has this court been in the construction of the statute, that it has held that unless the assignee transfers all the property to the debtor, the statute is inapplicable.

A consent to an equity receivership is *not* of necessity the surrender of all the corporate property. It is but the surrender of the property within the particular jurisdiction in which the suit has been filed. Attachments may be levied against property without the jurisdiction, because title thereto is still in the debtor.

Zacher vs. *Fidelity Trust, Etc. Co.*, 106 Fed., 593.

On no possible theory can it be held that the judgment creditor's suit is a voluntary assignment of the debtor's property.

The Admission of the Allegations of the Bill and the Consent to the Appointment of a receiver are not the commission of Acts of Bankruptcy within the meaning of Section 3466.

Whether the consent of the appointment of the re-

ceiver comes within the clause of R. S. 3466 "as well * * * as to cases in which an act of bankruptcy is committed," involves two questions:

(1) Has the defendant corporation committed an act of bankruptcy; and

(2) Even if it has, is the mere commission of an act of bankruptcy, not followed by any proceeding under a state insolvency law or a Federal bankruptcy act, sufficient to entitle the United States to a priority under Section 3466?

A.

The defendant has not committeed an Act of Bankruptcy within the Provisions of the Bankruptcy Act of 1898.

If an act of bankruptcy were committed under the bankruptcy act, it would of necessity under Section 3, have to be either a general assignment for the benefit of creditors, or

> "Being insolvent, applied for a receiver or trustee for his property, or because of insolvency a receiver or trustee has been put in charge of his property under the laws of a state, a territory or of the United States."

(1) It already has been shown that the present suit is not a general assignment.

(2) The receiver was not appointed *because of insolvency.*

The bill of complaint alleged that the defendant was solvent (R., p. 14). The answer admits the allegations. The purpose of the bill was to conserve the assets. The court did not appoint a permanent receiver, but merely a temporary receiver (p. 17) until a meeting of creditors (p. 19) and from time to time the temporary receiver-

ship was continued until more than three months after the filing of the bill, during which period the business was continued and attempts made to reorganize (p. 6). Then only were the assets liquidated (p. 6). These facts fail to show that the receiver was appointed because of insolvency.

By Section 1, subdivision 1 (a) (15):

> "A person shall be deemed insolvent within the provisions of this act whenever the aggregate of his property * * * shall not at a fair valuation be sufficient in amount to pay his debts."

There is no proof that this condition existed at the time of the filing of the bill or that the bill was filed *because* of this condition. This being so, the rulings of this Court of *United States* vs. *Oklahoma* and *Strain* vs. *United States* are conclusive to the effect that the receiver was not appointed because of insolvency. To the same effect are:

Matter of Spaulding, 139 Fed., 244;
Matter of Valentine Pohl Co., 224 Fed., 685;
Matter of William S. Butler & Co., 207 Fed., 705, certiorari denied 231 U. S., 752.

(3) The defendant has not, "*being insolvent*," applied for a receiver or a trustee for its property. The defendant did not apply for a receiver at all. It merely waived its right to have the suit brought by a judgment creditor. The fact that the defendant consented does not make the suit collusive or other than the ordinary law suit in which the defendant corporation is the defendant and not the plaintiff.

In re Metropolitan Railway Receivership, 208 U. S., 90.

This section of the Act was intended to cover cases where a plaintiff corporation instituted voluntary dissolution proceedings under State statutes or the like. There is also nothing to show that at the time the application was made, the defendant was in fact insolvent. (*United States* vs. *Oklahoma*).

B.

Even if the defendant did commit an Act of Bankruptcy under the 1898 Bankruptcy Act, the United States would not be entitled to priority, inasmuch as the defendant has not been divested of its property in any proceeding based upon the alleged act of bankruptcy.

While it is believed that it has been shown that no act of bankruptcy has been committed under the 1898 Act, it is nevertheless urged that even if such act of bankruptcy were committed, the mere commission of the act, not followed by a proceeding in bankruptcy based thereon, is insufficient to create the priority under Section 3466. Under Section 3467 there must be some assignee or Trustee who takes title to the assets and becomes Trustee for the United States. *Lewis* vs. *United States*, 92 U. S., 618, and cases *infra*. To make this entirely clear, it is necessary again to revert to the history of the Statute and its interpretation. The first Act of 1789 (1 Stat., 29), provided:

> "And in all cases of insolvency or where any estate in the hands of executors or administrators shall be insufficient to pay all the debts due from the deceased, the debt due to the United States on any such bonds shall be first satisfied."

It is clear that the words "cases of insolvency," as used in the original act, referred exclusively to cases arising in the insolvency or bankruptcy courts. In 1789, state insolvency and Poor Debtor Laws had been in effect and were well known, and the reference was to a

technical insolvency proceeding, under which the debtor was divested of his property.* This did not include general assignments or absconding debtors.

In 1792 the meaning of the term "insolvency" was extended, for the act provided:

> "That the cases of insolvency in the said 44th section mentioned shall be deemed *to extend as well* to cases in which a debtor not having sufficient property to pay all his or her debts shall have made a voluntary assignment thereof for the benefit of his or her creditors, or in which the estate and effects of an absconding, concealed or absent debtor shall have been attached by process of law, as to cases in which an act of legal bankruptcy shall have been committed."

Here for the first time is found the explanatory clause, which is substantially identical with that found in the present statute.

The 1792 Act provided new cases in which there was was to be priority. That is, there was to be priority in cases of insolvency, to wit, "legal bankruptcy," and

> "As well to cases where the debtor made the voluntary assignment and the case in which there was the absconding, concealed or absent debtor whose property was attached."

It is clear that the term "legal bankruptcy" had the same significance as the original Act of 1789 and was intended to refer to an insolvency proceeding as such.

Thus in *United States* vs. *Hooe*, 3 Cranch, 73, 90, Chief Justice Marshall said:

> "The whole explanation relates to such a general divestment of property as would in fact be equivalent to insolvency in its *technical sense*."

*See examples in *Sturges* vs. *Crowinshield*, 4 Wheat., 125, and *Ogden* vs. *Saunders*, 12 Wheat., 212.

And in *Thelusson* vs. *Smith,* 2 Wheat., 396, 422, the court said:

> "There can be little doubt but that the word insolvency mentioned in the act of 1790, ch. 35, par. 45, and repeated in the act of 1797, ch. 74, par. 5, and of 1799, ch. 128, par. 65, means a legal insolvency, which, whenever it occurs, the right of preference arises to the United States, as well as in the other specified cases to which the acts of 1797 and 1799 have extended the cases of insolvency."

In *Conard* vs. *Nicoll,* 4 Peters, 291, it appears that Judge Washington in the Circuit Court, in considering the meaning of the phrase under consideration, after pointing out that the expression insolvency extended to general assignments and to cases of attachment, stated (at p. 308) that it also extended:

> "3d. To cases in which an act of legal bankruptcy shall have been committed; that is, as the construction of the proviso in connection with the enacting clause seems necessarily to require, to cases where the property is in the hands of assignees, not by voluntary assignment only, but by assignment made in virtue of any state bankrupt law, or (possibly) of any bankrupt law of the United States which might thereafter be passed. There must be an assignment, either voluntary or compulsory, or else there can be no assignee, to be made liable to the United States, under the enacting clause. *If a mere act of bankruptcy be sufficient* to give rise to the preference of the United States from the moment of its commission, where is the assignee who is first to satisfy the claims of the United States out of the estate of the debtor, under the penalty, stated, in the enacting clause, of satisfying it out of his own estate. If it be said, that when the assignment of the bankrupt's estate shall be made, the preference of the United States will relate back to the act of bankruptcy, so as to overreach intermediate *bona fide* securities given by the insolvent to creditors,

> I can only answer that the assumption is altogether gratuitous, and receives no countenance from any part of this or any other act on this subject."

In the Supreme Court, the judgment was affirmed, this court saying:

> "This cause has been submitted, without argument. It is, in all its leading features, both in the points of law which arose and the evidence given at the trial, so similar to the case of *Conard* vs. *Atlantic Insurance Company*, decided by this court at January term, 1828, 1 Pet. 386, that we do not think it necessary to enter into an examination of the principles on which the judge submitted the cause to the jury. They appear to us to be in perfect accordance with the opinion delivered in that case, on great deliberation; of the entire correctness of which, we do not entertain a doubt."

And see to same effect *U. S.* vs. *Clark*, 1 Paine, 620, Federal case #14,807.

In *Beaston* vs. *Farmers' Bank*, 12 Pet., 102, 118, this Court says:

> "In giving a construction to these statutes, this court has held, that they only apply to two general classes of cases, viz: a living insolvent, *having an assignee;* and a dead insolvent, represented by executors or administrators (*Conrad* vs. *Nicoll*, 4 Pet., 308); that the priority, as against living debtors only existed where the debtor had become actually and notoriously insolvent, and being unable to pay his debts, has made a voluntary assignment of all his property; or, having absconded, or absented himself, his property has been attached by process of law. See *United States* vs. *Hooe*, 3 Cranch., 73; 1 Pet., 439. The words bankruptcy, and insolvency, mentioned in the statutes, are used as synonymous terms; and must be understood to apply to cases of insolvency *specified by the legislature;* and to mean a

> legal and known insolvency, manifested by some notorious act of the debtor, pursuant to law (*Prince* vs. *Bartlett*, 8 Cranch., 431); or where, by operation of law, the property of the debtor is taken out of his hands to be distributed by others (*United States* vs. *Clark*, 1 Paine, 629; and see *Thelusson* vs. *Smith*, 2 Wheat., 396); or where the property is in the hands of assignees, not by voluntary assignment only, *but by assignment made in virtue of any state bankrupt law, or, possibly, of any bankrupt law of the United States, which might hereafter be passed. Conrad* vs. *Nicoll*, 4 Pet., 308. It is not a mere inability of the debtor to pay all his debts, but that inability must be manifested in one of the three modes pointed out in the explanatory clause of the section. 1 Pet., 439."

These cases make it clear that the amendment of 1792 simply extended the term "cases of insolvency" to two new cases, namely, general assignments and absconding debtors, and that the phrase "as to cases in which an act of legal bankruptcy shall be committed" was not a new case but merely a paraphrase of the original "cases of insolvency" which, as already shown, referred to a proceeding under a State or possibly future insolvency law.

It hardly needs argument to show that a judgment creditor's bill, even as extended to include the rights of creditors other than the original plaintiff,* is not a proceeding under an insolvency or bankruptcy act, but is the mere exercise of the inherent power of the Court of Chancery. Nowhere is this made clearer than in the opinion of Chief Justice Shaw in *Commonwealth* vs. *Phenix Bank*, 11 Metcalf, 129, where he said in a proceeding brought by a State against the bank under a state statute:

> "It has sometimes been said that this was a law providing a mode by which banks can be placed in a state of legal insolvency, or in other

*The "amount in controversy is still the amount of plaintiff's claim alone—*Karatz* case, 262 U. S., 77, 86.

words an insolvent law for banks. This seems to arise from too hasty a conclusion that, because things are alike in many respects, they are alike in all. The most that can be said of the act in this respect is, that it is like an insolvent law for banks, because it may so operate as to put an end to the further operation of the bank, in case of insolvency, distribute the whole of its funds amongst creditors and stockholders, and thus operate like a bankrupt law or insolvent law. * * * But it does not necessarily, and will not, perhaps, generally have this operation; and it differs from an insolvent law in this, that the object of the act is not to declare the bank insolvent or to effect any transfer or assignment of its property. It provides for a chancery proceeding by which a competent judicial tribunal is authorized to regulate the proceedings of a bank by an injunction, temporary or permanent, absolute or qualified, effecting all their proceedings, or some particular proceeding only, according to the exigencies and peculiarities of each particular case. * * * The power vested in the court has been exercised by a view to accomplish the object contemplated by the statute, according to the exigencies of each particular case, without regard to the consideration whether it would lead to the final termination of the affairs of the bank or not. Even when receivers are appointed, they are to be appointed as receivers in a proceeding directed to be conducted 'according to the course of chancery proceeding.' They are officers of the law, subject in all respects to the orders and directions of the court. The law requires no assignment to be made to them, either by the bank or by any authorized court or officer. In practice, none is usually made, and none has been made in this case. They are to take possession of the property and effects of the corporation, subject to the rules and orders of the court. Their power to sell and convert the property into money is not given them by statute, or by any assignment or transfer, but it depends wholly on the order of the court. The distribution of the proceeds among bill holders and other creditors, and the residue,

> if any, to stockholders—a feature so essential to every system of bankrupt or insolvent laws—is not provided by this statute, but results only from the orders and decrees of the court, regulated by those principles of equity which govern all courts in the disposition of funds directed to be administered according to the course of chancery proceedings. Although, therefore, the proceedings under this law, in their ultimate results, and in some states of facts, operate like an insolvent law for this class of corporations, that is not the declared or obvious purpose nor the necessary consequence of the law. And further, it is wanting in the most essential feature of an insolvent law, that of divesting the debtor of the property, and vesting it in some other person, and constituting the proceeds a trust fund for creditors, in which it is held that the United States, as *cestui que* trust have a priority for the payment of their whole debt. It is therefore not a case of legal bankruptcy or insolvency; for we believe these terms as used in this sense are synonymous within the construction of the United States St. of 1797, c. 774."

That the appointment of a receiver on a judgment creditor's bill is not a divesting of the debtor's title to all his property within the purview of the Act is also held in *Beaston* vs. *Farmers' Bank*, 12 Peters, 102. There receivers were appointed in a suit by the United States as a judgment creditor with authority to take possession of the property of a bank, to dispose of the same and to collect all debts. The court held that even if the receivers had taken possession, there would not have been a transfer and possession of the property of the bank within the meaning of the Act of 1797. The court said at 12 Peters, 102, 136:

> "We are next to inquire into the legal effect of the appointment of receivers by the Circuit Court. Without deciding whether a circuit court of the United States has authority, in a case like this, to appoint receivers with power to take possession

> of all the property of a debtor of the United States, it is sufficient to say in this case that it does not appear that the power conferred on the receivers was ever executed; *and if it had been, it would not have been a transfer and possession of the property of the Elkton Bank, within the meaning of the act of Congress, and, therefore, the priority could not have attached to the funds in their hands.*"

These cases all clearly indicate that the mere commission of an *act* which would be ground for the filing of a bankruptcy petition, is not sufficient to divest the debtor of his property or to create a priority, and accordingly, even if the consent to the equity receivership were an act of bankruptcy, so as to create the *right* to file a petition, it is not an *act* of bankruptcy within the meaning of the Act of 1797 or the successor act, Section 3466.

These cases also show that the Act of Bankruptcy referred to in 3466 refers exclusively to proceedings under a bankrupt or insolvent statute and that that section can have no application to the exercise by a Court of Chancery of its inherent powers under a judgment creditor's bill.

If it is an act of bankruptcy which would be a ground for the filing of a petition, and, therefore, would give rise to a priority for an ordinary debt under 3466, *the remarkable situation would be presented, that if a debtor was adjudged a bankrupt, ordinary debts due the United States would be entitled to no priority under the recent decision of this Court in Davis* vs. *Pringle,* 69 *L., Ed.,* 645, *but if the same debtor merely committed an act of bankruptcy and was not thereafter adjudged a bankrupt, there would be a priority.*

This construction of Section 3466, insofar as ordinary debts are concerned, will bring the provisions of that Section into harmony with the Bankruptcy Act of 1898 as construed in *Davis* vs. *Pringle.* That is to say, if a debtor of the United States merely commits an act of bankruptcy, which may be the ground of the filing of an

involuntary petition, there is no priority for ordinary debts, for the debtor has not been divested of title to his property. If, however, he commits an act of bankruptcy and goes into bankruptcy, then the provisions of the Bankruptcy Act must be applied and under *Davis* vs. *Pringle,* and there also would be no priority. If this were not so, as above pointed out, there would be priority for the United States if a mere act of bankruptcy were committed, but no priority if the debtor went into bankruptcy.

Of course, the situation with respect to taxes is somewhat different. That fact cannot change the conclusion that the phrase "act of bankruptcy" in 3466 means actually going into bankruptcy. With respect to taxes, the foregoing consideration would lead to this result. Where the debtor is indebted for taxes and merely commits an act of bankruptcy and does not go into bankruptcy, there is no priority, but if the act of bankruptcy is followed by an adjudication in bankruptcy, then by virtue of the provisions of Section 64 of the Bankruptcy Act, there would be a priority.

In this situation, it simply means that under existing statutes if the debtor has committed an act of bankruptcy and the Government seeks a priority for its taxes, it may obtain a lien on the assets pursuant to R. S., Section 3186.

Of course, it may well be doubted whether at the present time there should be any priority for taxes in an insolvency proceeding, *at the expense of the particular creditors* where the taxes were not assessed until after the filing of the petition.

As stated by Mr. Justice HOLMES in *Davis* vs. *Pringle* (69 L. Ed. at 647):

> "Public opinion as to the peculiar rights and preferences due to the sovereign has changed."

It may be that the same change in public opinion has occurred respecting taxes first found to be due after in-

solvency. Upon this question there is no doubt a difference of opinion. It is in any event a legislative question. Whether, therefore, the provisions of the bankruptcy law directing the prior payment of taxes should be extended to all kinds of proceedings is a question which must be left to the discretion of Congress.

It appears, therefore, that the defendant corporation was not divested of title to his property by the appointment of the equity receiver; that it did not make a voluntary assignment of its property and that it has not been thrown into bankruptcy or filed a voluntary petition, and, accordingly, there has been committed no "act of bankruptcy." This being so, no priority exists.

POINT VI.

Congress has by the Revised Statutes provided a comprehensive method for the collection of taxes and has provided for a lien and distraint, and as the provisions of Revised Statutes 3186 et seq. as amended in 1913 were not complied with in this case prior to the receivership, a tax claim is not entitled to priority.

In recognition of the fact that the sovereign priority did not devolve upon the Federal Government and that there was no right to issue the writ of extent, as in England,* Congress as a part of the income tax law passed immediately following the Civil War, provided for a lien for taxes after notice and demand, and in detail for the issuance of warrants and distraints. These provisions are now Sections 3186, *et. seq.*, of the Revised Statutes. These provisions, together with the priority created by Section 3466 in the specific cases therein indicated, were deemed sufficient to protect the public revenues. These *two statutes are the equivalent of the two common law prerogatives* (page 8, *supra*).

*Marshall vs. New York, 254 U. S., 380, 382, *supra*, p. 9.

By amendment to Section 3186 in 1913 (37 Stat. Part 1, p. 1016) the lien of the United States for taxes was declared not to be good as against subsequent purchasers, mortgagees or judgment creditors, unless filed as the statute directed (See Statute, page 5 *supra*).

In the present case the tax was not assessed until after the receiver was appointed and the property of the defendant had passed into the custody of the court. At the time of the filing of the bill, there was no lien. However, if the contention of the Government is sound, it must be held that if Mears, the plaintiff in this case, had obtained a judgment, had execution returned unsatisfied and had brought a judgment creditor's bill, the Government would have a priority over Mears' judgment, despite the fact that the provisions of 3186 had not been complied with. *If it be true that the United States has such a priority, then the provisions of 3186 insofar as they protect the rights of judgment creditors, are wholly meaningless.*

If numerous other creditors of the defendant corporation had instituted suits, obtained judgments and eventually brought judgment creditors' suits, their right of satisfying such judgment out of the assets of the defendant would have been superior to that of the Government, because of the latter's failure to comply with Section 3186. The government would have had no priority. The fact that the suit was instituted by one creditor, Mears, on behalf of all, and the fact that a judgment was waived and the other creditors enjoined from proceeding to judgment, cannot increase the rights of the United States.

See *American & British Securities Co.* vs. *American & British Manufacturing Co.*, 275 Fed., 121.

This suit is a mere equitable levy in favor of all creditors (*Pa. Steel Co.* vs. *N. Y. City Ry.*, 198 Fed., 721, 737,

supra), and they all have the same rights as they would have had if they were separate judgment creditors, namely the right to satisfy their claims ahead of the Government because the latter did not comply with Sec. 3186 as amended in 1913. As the two common law prerogatives are embodied in Section 3466 and Sections 3186 et seq., and as no priority exists under the terms of either, there can be no priority at all.

POINT VII.

The Federal officials charged with the duty of collecting the internal revenue have always practically construed Sections 3466 and 3467 to include claims for taxes and have heretofore always asserted the right to priority and the right to hold executors and trustees personally liable, solely because of the provisions of those sections. The proof of claim in this very case bases the right of priority and the alleged obligation of the receiver upon the provisions of the statute. This practical construction should not be disturbed, except for very cogent reasons.

There is not the slightest indication in the reported cases or elsewhere that the government officials have heretofore relied upon an inherent sovereign priority for the payment of taxes. The proof of claim filed in this very case (R., pp. 7 and 8) asserts that the priority is fully determined by Section 3466 of the Revised Statutes, and the proof of claim states further (R., p. 8):

> "That no security therefore is held by the United States and that there are no set-offs or counterclaims.

"That this claim is entitled to be paid before all other claims, the priority of the United States for the payment of taxes being fully determined by Section 3466 of the Revised Statutes and Section 64 (a) of the Bankruptcy Act.

"And attention is hereby called to Section 3467 of the Revised Statutes which provides that every executor, administrator, or assignee, or other person who pays any debt due by the person or estate from whom or for which he acts, before he satisfies and pays the debts due to the United States from such person or estate, shall become answerable in his own person and estate for the debts so due to the United States, or for so much thereof as may remain due and unpaid."

If these sections, as is now contended, have no relation to taxes, then there can be no personal liability of the receiver, as is indicated in the proof of claim.

An examination of proofs of claim for taxes filed in numerous other equity receiverships indicates that in all the Government bases its right to priority on the express provisions either of Section 3466 or on the Bankruptcy Act. It is only when it is argued that priority created by 3466 does not cover the case of a judgment creditor's bill, that the government abandons its claim that it is entitled to hold trustees personally liable by virtue of the statute, and falls back upon a supposed inherent priority, the existence of which never before has been asserted. This practical construction of the source of the Government's alleged rights and this interpretation of the statute by the executive department and by officials charged with the enforcement of the law, is entitled to great weight and is not to be disturbed, except for very cogent reasons.

Swendig vs. *Washington Council*, 265 U. S., 322, 331.

POINT VIII.

The decree appealed from should be reversed and a decree directed which shall adjudge that the claims of the United States for taxes and for duties are not entitled to priority; that the United States is a general creditor of the defendant and that the Receiver is entitled to retain as a setoff against all dividends heretofore or hereafter declared upon the Government's claims, dividends up to the sum of $3,149.91.

Respectfully submitted,

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